

OFFICE OF THE CITY CONTROLLER



**FISCAL YEAR 2016
UPDATED AUDIT PLAN**

Ronald C. Green, City Controller

Courtney E. Smith, City Auditor



OFFICE OF THE CITY CONTROLLER
CITY OF HOUSTON
TEXAS

RONALD C. GREEN

September 4, 2015

The Honorable Annise D. Parker, Mayor
City Council Members
City of Houston, Texas

SUBJECT: Office of the City Controller
Updated Fiscal Year 2016 Audit Plan

Dear Mayor Parker and Council Members:

I am pleased to submit to you the Updated Fiscal Year 2016 Audit Plan. The basis of this year's Annual Audit Plan (Audit Plan) was the 2014 Enterprise Risk Assessment (ERA) performed by the Audit Division as required. Additional consideration is given to input from your Office, City Council Members, and Department Directors. This document will serve as the primary work plan to carry out the audit responsibilities in an efficient and effective manner. To enhance our effectiveness, our approach is balanced by conducting the audits using, in-house staff and by co-sourcing or outsourcing some projects requiring certain technical or specialized skills.

This Audit Plan includes performance, compliance/contract, monitoring, continuous auditing, and unannounced audits. Additionally, the plan provides for follow-up procedures and special projects.

We post the status of progress in executing our audit plan on a quarterly basis on the Audit Division webpage within the Office of the City Controller website.

Respectfully submitted,

Ronald C. Green
City Controller

Xc: Christopher Newport, Chief of Staff, Mayor's Office
Andy Icken, Chief Development Officer, Mayor's Office
Department Directors



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BACKGROUND AND AUTHORITY –

The City Controller is an independently elected official who is granted authority through the Article VIII of the City Charter. Article VIII, Section 7, *Audits*, requires the City Controller to “... be responsible for conducting internal audits, in accordance with professionally recognized auditing standards, of the operations of all City departments, offices, agencies and programs. The scope of internal auditing shall encompass an objective and systematic examination of evidence to provide an independent assessment of the efficiency and effectiveness of the city's system of internal controls and the quality of performance based on quantifiable criteria in meeting objectives....”. The City Controller assigns this responsibility to the City Auditor (through appointment) to be the executive in charge of the Audit Division, whose scope of work is contained under a separate Charter (Audit Division Charter). Audit results are issued to the Mayor, City Council Members and Department Directors.

AUDIT DIVISION ORGANIZATION –

At the end of FY2015, the Audit Division had a total headcount of 10, consisting of 8 professional audit staff, one support staff, and the City Auditor. Audit Division staff provide audit related services as their primary focus. Additional training, certifications, and experience will enhance staff ability to provide services.

The Controller's Office utilizes internal and external audit resources to execute our mission and objectives and meet the needs and requests of our varied stakeholders. We currently have 8 professional service firms under contracts which will expire March 15, 2016.

APPROACH AND METHODOLOGY –

The Audit Division adheres to: 1) the *Government Auditing Standards* (GAS – commonly referred to as the “Yellowbook”) as promulgated by the Government Accountability Office (GAO) and 2) the International Standards for the Professional Practice of Internal Auditing as issued by the Institute of Internal Auditors (IIA – known as the “Redbook”). To assure compliance with these professional standards, the Audit Division undergoes a peer review every 3 years. The most recent peer review was completed November 1, 2013.¹

The Annual Audit Plan is a *flexible* commitment of the Audit Division within the Office of the City Controller which establishes areas that will be prioritized for audits in accordance with the responsibility and authority identified in the City Charter. The Audit Plan, approved by the City Controller, serves as a working document that considers items such as; the Enterprise Risk Assessment (ERA), input from the Mayor, City Council, Department Management, and results from previous audits. Due to continual requests for audit services, the increasing demand for non-audit services, and the required testing for planned activities, the Audit Plan will be monitored and revised as necessary throughout the year.

The professional standards noted previously require that the Audit Plan be grounded in risk-based methodology. An Enterprise Risk Assessment (ERA) is conducted annually on selected Departments on a rotational basis for efficiency and to ensure full coverage of all City Departments over a 4-5 year period².

Evaluation of these factors provides indicators for prioritizing potential projects for the upcoming year. In other words, this points us in the direction of “*what*” to audit. We then identify the available resources to determine the volume of activity to include in our plan (see Audit Resource Allocation section below).

¹ See 2013 Peer Review reports at <http://www.houstontx.gov/controller/audit/peerreview.html>

² See 2015-08 FY2014 ERA Update under separate cover.



AUDIT RESOURCE ALLOCATION –

Annually, the Audit Plan prioritizes the Audit Division's limited resources of budgeted staff and funds based on the ERA. The Audit Plan, therefore prioritizes expending efforts on either common Key Business Processes or Departments having a perceived high or moderate risk profile rating. Specific risk factors related to internal controls, estimated liability, and levels of exposure are used to identify and prioritize risks. As such, the City's audit function serves as a risk evaluation resource.

The number of projects that are proposed is based on consideration and an evaluation of:

- Current headcount within the Audit Division;
- Average number of hours used on a typical audit engagement³;
- Other types of ongoing services that the Controller's Office provides; and
- Unplanned requests from Mayor, City Council, or other Department Management,

USE OF EXTERNAL CONSULTANTS

For projects that involve circumstances where; 1) The use of experts/specialists is required; 2.) The independence of the Audit Division as an organization is impaired; or 3.) There is the potential for significant political sensitivity, the Office of the City Controller may elect to use external consultants. NOTE: A budgeted dollar amount is approved for the use of these resources.

AUDIT PROGRAMS –

Upon the City Controller's approval of the Audit Plan, specific audit programs will be developed for each activity to be audited within the fiscal year ending June 30, 2016. The audit programs will be designed with regard to business services, compliance and other requirements, performance considerations, management input, and specialized skills in order to meet the specific audit objectives of each project. All audit programs, workpapers, and reports will be prepared in accordance with:

- Relevant standards issued by the American Institute of Certified Public Accountants;
- Government Auditing Standards (*Yellow Book*); and
- The Institute of Internal Auditor's International Standards for the Practice of Internal Auditing (*Red Book*).

Where applicable, disclosure of nonconformance will be provided.

STATUS AND UPDATES TO ANNUAL AUDIT PLAN –

The specific projects conducted throughout the year may be a sub-set of the list provided in the Audit Plan. The nature, extent, and timing of audit activities will vary as a result of the differences in the nature of operations, organizational structure, and resource availability.

The Audit Division will also provide any assistance to City's management or City Council when they request special projects (*assuming the available resources exist, and depending on the context and priority of the assignment as it relates to risk, exposure, fraud, waste and/or abuse*). These special projects will normally be performed in addition to planned audit work. If the assistance requires the use of external consultants, additional funds may need to be provided by the appropriate departments and/or City Council.

³ The Audit Division is a member of the Association of Local Government Auditors (ALGA), which provides aggregated data on internal auditing for local governments, including resource utilization (average number of hours per project).



Executing the Audit Plan involves an update and status process that is scheduled weekly between the City Auditor and the City Controller. Additionally, the Audit Division posts a high-level status report on the Audit Division's website, accessible from the City Controller's Webpage. Feedback to the Division in the form of Post-Audit Surveys and Requests for Audit Services is also available from the Audit Division's website.⁴

ANTICIPATED BENEFITS OF AUDIT ACTIVITIES –

Compliance



Improve Accountability



Cost Savings



Improve Risk Management
and Internal Controls



Improve
Financial Reporting



Improve Efficiency



⁴ The Audit Division has a website accessible from the Controller's website, which post results of audits, follow-up procedures, and status of progress. See: <http://www.houstontx.gov/controller/audit>



FISCAL YEAR 2016 PLANNED ACTIVITY (PROJECTS)

The following is a list of projects for the FY 2016 Annual Audit Plan. The Audit Process is often thought to be linear in nature however it is a dynamic process and adjusts to evidence, impact, and magnitude of discovery as it occurs during the engagement process. The list provided is the population of projects from which the Audit Division will execute. The status/progress of projects on the Annual Audit Plan is posted on the Audit Division website. In addition, the Audit Division personnel meet with the City Controller weekly to provide a level of transparency and accountability for meeting our goals and objectives.

COMPLIANCE/PERFORMANCE/FINANCIAL AUDITS AND PROCESS REVIEWS

The following projects are planned to begin during FY2016:

ADMINISTRATIVE AND REGULATORY AFFAIRS (ARA)

PROCESS REVIEW – BARC CASH HANDLING PROCESSES

DESCRIPTION: Review and test internal controls in place for handling cash to ensure City assets are safeguarded and managed appropriately.

ECONOMIC DEVELOPMENT (MYR/PD)

PERFORMANCE/COMPLIANCE AUDIT – CHAPTER 380 PROGRAM REVIEW

DESCRIPTION: The Texas State Legislature passed Chapter 380 of the Texas Local Government Code, which authorizes municipalities to establish Chapter 380 Programs. The City of Houston has executed several Chapter 380 agreements. The Audit Team will review the collective status of the agreements and select specific agreements for further independent review.

ECONOMIC DEVELOPMENT (HCDD/MYR)

PERFORMANCE/COMPLIANCE AUDIT – TAX INCREMENT REINVESTMENT ZONE (TIRZ) FUND

DESCRIPTION: Tax Increment Reinvestment Zones (TIRZs) are special zones created by City Council to attract new investment to a specific geographical area. The zones are designed to help finance the cost of redevelopment and encourage development in an area that otherwise would not attract sufficient market development. The audit team will review controls in place and determine if transactions in TIRZ Fund 2409 managed by HCDD, were made in accordance with the specific purposes allowed by applicable policies, laws, regulations and ordinances.

HEALTH AND HUMAN SERVICES (HHS)

PROCESS REVIEW – CASH HANDLING PROCESSES

DESCRIPTION: Review and test internal controls in place for handling cash to ensure City assets are safeguarded and managed appropriately.



HOUSTON INFORMATION TECHNOLOGY SERVICES (HITS) – (CO-SOURCE)

PERFORMANCE/PROCESS REVIEW – CITYWIDE CLOUD APPLICATIONS

DESCRIPTION: Houston Information Technology Services (HITS) was created to improve the IT organization throughout the City and provide guidance in the wake of technological advances. The audit team will review the extent of cloud service use, internal controls, and safeguards in place to evaluate cloud applications and minimize cybersecurity threats to the City's networks.

HOUSTON PERMITTING CENTER (HPC) - ADMINISTRATION AND REGULATORY AFFAIRS DEPARTMENT (ARA)

PERFORMANCE/COMPLIANCE AUDIT – PERMITTING OPERATIONS

DESCRIPTION: The HPC is responsible for the administration and enforcement of more than 600 permits, licenses, and registrations. Permitting, licensing, and registration activity can be done in person at HPC and some permits are available for purchase online. The audit team will review and validate compliance of selected permitting activity with applicable ordinance and/or regulatory terms and the effectiveness of controls over processing permits and the collection of permit revenue.

HOUSTON POLICE DEPARTMENT (HPD)

PERFORMANCE/COMPLIANCE AUDIT – PROPERTY/EVIDENCE ROOM

DESCRIPTION: HPD uses an Evidence Management System (EMS) and relocated the property room in conjunction with the implementation of the system. This audit team will focus on ensuring the accuracy of the EMS and compliance with their policy and procedures.

MUNICIPAL COURTS DEPARTMENT (MC)

PERFORMANCE/COMPLIANCE AUDIT – CSMART APPLICATION AND CASH MANAGEMENT

DESCRIPTION: City of Houston Municipal Courts is one of the largest municipal court systems in the United States, adjudicating over 500,000 cases each fiscal year. The audit team will evaluate internal controls over collection processes for fines and fees, recording of payment activity, procedures for safeguarding cash collections, and the proper recording of non-cash transactions that result in final case dispositions.

OFFICE OF BUSINESS OPPORTUNITY (OBO)

PERFORMANCE/COMPLIANCE AUDIT – PAY OR PLAY

DESCRIPTION: The Office of Business Opportunity administers the Pay or Play (POP) program implemented through Executive Order 1-7. The program seeks to promote an environment that fosters a quality workforce for employees working on City contracts. The audit will evaluate whether funds are accounted for appropriately and deposited timely.



PARKS AND RECREATION (PARC) – CASH HANDLING AND INVENTORY CONTROL PROCESS REVIEW

PROCESS REVIEW – CASH HANDLING PROCESSES

DESCRIPTION: Review cash handling processes and internal controls in place over inventory at City operated Golf Courses to ensure City assets are safeguarded and managed appropriately.

CARRYOVER AUDITS FROM FY2015 AUDIT PLAN COMPLETION ORDER

The following projects were in progress during FY2015 and are being completed in FY2016:

ADMINISTRATION AND REGULATORY AFFAIRS (ARA)

PERFORMANCE/COMPLIANCE AUDIT – PARKING MANAGEMENT

DESCRIPTION: Parking operations are administered and enforced by the Parking Management Division as set by the Traffic Engineer. The Division also manages the collection of parking rates set by the Mayor, City Council, and the Parking Commission. The audit will assess operational compliance with applicable ordinances, regulations, and/or guidelines and the controls governing the timely and accurate collection and recording of parking related revenue.

CITY-WIDE POLICY FRAMEWORK

PERFORMANCE/COMPLIANCE AUDIT AND EFFICIENCY OF DESIGN REVIEW – CITY WIDE ADMINISTRATIVE PROCEDURES, EXECUTIVE ORDERS, AND MAYOR’S POLICIES

DESCRIPTION: Policy and procedures are created by management to outline a framework to direct behavior in alignment with mission and objectives significant to the operations as it defines the internal controls to mitigate risks associated with processes, resources, laws and regulations. The Audit Team has developed a strategy to gain coverage of auditing for compliance and the overall design as it pertains to management objectives.

FLEET MANAGEMENT DEPARTMENT (FMD)

PERFORMANCE / CONTRACT COMPLIANCE – VEHICLE REPLACEMENT PART SUPPLY CONTRACT WITH NAPA

DESCRIPTION: Several City Departments acquire, maintain, and dispose fleet vehicles that vary from standard automobiles (fuel, hybrid, and electric), trucks (pick-up, straight, dump, etc.), heavy equipment, and specialized vehicles for specific purposes (Fire, Emergency Medical Transportation, Waste, etc.). During FY2011 Fleet Management functions from various departments were consolidated into a newly formed Fleet Management Department. The process for managing spare/replacement parts inventory was outsourced to the Genuine Parts Company (NAPA) as supported by City contract #4600010761. The total contract value was \$95 million over a 5 year term. Since the inception of the contract, the City has paid the vendor approximately \$35 million. The audit will focus on compliance with key contract terms and management controls in place to monitor the contract activity, spending, and efficiency.



GENERAL SERVICES DEPARTMENT (GSD)

PERFORMANCE/CONTRACT COMPLIANCE AUDIT – BUILDING AND MAINTENANCE SERVICES CONTRACT – MCLEMORE

DESCRIPTION: The City utilizes an external vendor to perform some of the building maintenance services for various departments. During FY2013 two contracts were renewed with a long-term vendor for four departments which totals approximately \$3 million. The audit team will review and validate compliance with key terms and conditions of these agreements.

HOUSTON AIRPORT SYSTEM (HAS)

CONTRACT COMPLIANCE AUDIT – CONSTRUCTION CONTRACT - CLARK CONSTRUCTION COMPANY

Description: HAS engages in significant contract activity for airport, terminal, facilities, security, maintenance, improvements, and repairs. One construction contract type that has potential for cost recovery and effective partnership is referred to as a Construction Manager at Risk (CMAR). During FY2011, the Office of the City controller performed an audit of Phase 1 of Project 417F which utilized Clark Construction Company as the CMAR. The project has been completed in two additional phases. The Audit Team will perform a closeout audit of the remaining activity that applies to Phase II and III which approximates \$100 million in project costs.

HOUSTON POLICE DEPARTMENT (HPD)

PERFORMANCE/CONTRACT COMPLIANCE AUDIT – CHILD SAFETY FUND

DESCRIPTION: HPD administers the Child Safety Fund through which funding is provided to local school districts to provide funding for school crossing guards. The audit will review and validate compliance with contract terms and verify that dollars provided under the contract are being utilized appropriately.

INFORMATION TECHNOLOGY DEPARTMENT (ITD) – (OUTSOURCED)

CONTRACT COMPLIANCE – LOCAL TELECOM EXPENSE (LANDLINES ONLY)

DESCRIPTION: The City spends approximately \$10 - 12 Million per year on local landline telephone services. The rates for services are per contract and subject to tariffs. The audit tested existence of lines being charged and the accuracy of the charges per the agreement or the appropriate tariff/rate.



ALTERNATIVE AUDIT PROJECTS FY2016

The Audit Plan is flexible based on changes to scope, staffing, access to information and other factors. Time and resources permitting, the following projects may be substituted for or performed in addition to the previously identified projects.

ADMINISTRATIVE AND REGULATORY AFFAIRS (ARA)

PERFORMANCE/COMPLIANCE AUDIT – PAYROLL APPLICATION SECURITY CONTROLS REVIEW

DESCRIPTION: ARA's Payroll Services Division is responsible for bi-weekly remuneration of City employees. The audit team will review general and application controls within the City's Payroll application to determine if they are adequate and in compliance with policies and other directives.

ADMINISTRATION AND REGULATORY AFFAIRS (ARA)

COMPLIANCE AUDIT – BARC PROCUREMENT COMPLIANCE

DESCRIPTION: BARC manages the City's animal shelter and adoption facility and provides veterinary care to animals brought in to the shelter. The audit will evaluate compliance with applicable policies, procedures, legislative and regulatory requirements.

FINANCE DEPARTMENT (FIN)

PERFORMANCE/COMPLIANCE AUDIT – DELINQUENT ACCOUNT COLLECTION CONTRACT AUDIT

DESCRIPTION: The City is engaged in a contract with an external professional service firm to perform collection activity on its behalf. The audit team will focus on compliance with key contract terms and conditions, and management controls in place to monitor collection activity.

HOUSTON AIRPORT SYSTEM (HAS)

CONTRACT COMPLIANCE AUDIT – CONSTRUCTION CONTRACT – WILLIAM P. HOBBY AIRPORT

DESCRIPTION: HAS engages in significant contract activity for airport, terminal, facilities, security, maintenance, improvements, and repairs. One construction contract type that has potential for cost recovery and effective partnership is referred to as a Construction Manager at Risk (CMAR). During FY2014, the City contracted with Hensel Phelps/CBIC (joint venture) for construction services at William P. Hobby Airport. The audit team will review contract requirements and performance measures to ensure compliance with contract terms.

HOUSTON FIRST CORPORATION

PERFORMANCE/CONTRACT COMPLIANCE AUDIT – CONTRACT COMPLIANCE

DESCRIPTION: Houston First Corporation, a local government corporation, operates convention and fine arts venues and parking garages with the mission to enhance quality of life and advance economic development for the City of Houston. The audit will review key terms of the Interlocal and lease agreements to ensure compliance with contract terms.



HUMAN RESOURCES (HR) –

PERFORMANCE/CONTRACT COMPLIANCE AUDIT – TEMPORARY SERVICES

DESCRIPTION: HR manages contracts related to temporary personnel services for the City. Citywide expenditures range from \$13 million to \$17 million. The audit will focus on compliance with contract rates and terms, billing accuracy, and change order processes.

CITIZEN CENTRIC REPORTING (CCR)

DESCRIPTION: The Association of Government Accountants (AGA) posts condensed reports of jurisdictions aimed at being “user” or constituent-friendly. The Comprehensive Annual Financial Report (CAFR) contains a wealth of financial, demographic, performance, and disclosure information and typically exceeds 300 pages. The goal of the CCR is to select key information (quantitative and qualitative) about the governmental entity and present it in a four-six page synopsis. The report generally includes visual presentation aids, such as charts, graphs, tables, etc. The professional staff assigned to this project will create a CCR for the City of Houston and post publicly on the Controller’s website and the AGA website.



SPECIAL PROJECTS & ONGOING MONITORING PROCEDURES

ENTERPRISE RISK ASSESSMENT (ERA)

DESCRIPTION: Each year the Audit Division develops the Audit Plan based upon risk (primarily business, financial, operational, etc.) Key benefits include; gains in significant knowledge, goodwill, and succession planning by having a diverse team exposed to all the major operations of the City. Professional auditing standards (both GAO and IIA) require audit resources to be allocated to projects based on continued risk assessment methodology. There are currently 4 major components to the ERA Process (1) Review of selected departments on a rotational basis, (2) Significant Events occurring during the FY, (3) Changes to major process, structure, leadership within the City, (4) Consideration of Information Systems.

FOLLOW-UP PROCEDURES

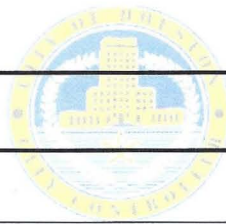
DESCRIPTION: As issues are identified during the course of conducting audits/engagements, they are documented and reported accordingly. In order to help initiate change and continued improvement, we communicate with responsible management at regular intervals, and obtain a status of progress on implementation of corrective actions. These communications are formally documented. Additionally, samples of items are tested on a periodic basis, depending on the magnitude, impact, and cost-savings with the results being published as formal reports that disclose status of open items and assess the overall remediation process employed by management.

FRAUD HOTLINE/REPORTING

DESCRIPTION: The Office of the City Controller provides two primary vehicles for reporting fraud, waste and/or abuse: (1) A Fraud Hotline answered by the Audit Division and (2) a link to report fraud available from both the Controller's Homepage and the Audit Division's Website. Additionally, the Audit Division provides auditing support based on requests from the OIG and/or other authorities. Each reported concern is addressed. This may result in performing substantive procedures, such as an audit, or may be referred to an outside agency or department for follow-up. The initial contact, work performed, conclusions and/or referral are documented to support their disposition. In some instances, this may also require subsequent follow-up or monitoring to adequately resolve. Consideration of Fraud Reporting is performed by the Audit Division on a regular basis and has direct involvement by professional staff that are Certified Fraud Examiners.

QUALITY ASSURANCE PROCEDURES

DESCRIPTION: Professional standards require that the audit function have a system of quality control/assurance in place to ensure all necessary elements are in place and operating effectively. Each audit/project is reviewed by a professional staff not directly assigned to the audit. The goal is to verify that sufficient, appropriate evidence is gathered and documented do adequately support conclusions based on procedures that are designed to test relevant audit objectives (this includes consideration of Fraud, professional judgment, competency, and supervision).



UNANNOUNCED AUDITS

DESCRIPTION: The Audit Division may perform audits on an unannounced basis during the year. These may include:

- Compliance with Specific Administrative Procedures or Executive Orders
- Petty Cash Counts;
- Inventory Audits (Test Counts/Controls)

A handwritten signature in blue ink, appearing to read "Courtney E. Smith".

Courtney E. Smith, CPA, CIA, CFE
City Auditor